

# REGULATION OF CHARITIES BY THE CALIFORNIA ATTORNEY GENERAL



# Overview

- ★ AG has primary responsibility for oversight of charitable trusts and solicitations
  - Including charitable corporations, unincorporated associations and charitable trustees and for-profit fundraising professionals

# Overview

- ✱ Charitable Trusts Section carries out AG mandate
- ✱ Composed of
  - ✱ Legal and Audit Unit
  - ✱ Registry of Charitable Trusts

# The Registry's Role

- ✴ Manages registration and annual reporting requirements
  - ✴ Initial registration within 30 days of receiving assets
  - ✴ Annual reporting (usually 990 and RRF-1)
  - ✴ Exempt from registration and reporting but not oversight: religious corporations, educational institutions, hospitals, health care service plans
- ✴ Responsible for receipt and review of notices of specific transactions charitable corporations required to submit to AG,\* including:

\*See Corp. Code sec. 5000 et seq.

# The Registry's Role

- Sale or disposition of substantially all assets
- Voluntary dissolution
- Merger
- Conversion to mutual benefit or business corporation
- Self-dealing transactions
- Loans to directors/officers
- Sale/transfer of nonprofit hospital facilities

# Transactions Requiring AG Notice or Consent\*

## ☀ Consent:

- ☀ Voluntary dissolution – requires AG waiver of notice
- ☀ Conversion to mutual benefit or business corporation
- ☀ Loans to directors and officers (with exceptions)
- ☀ Sale or transfer of nonprofit health facility

## ☀ 20-Day Notice Only:

- ☀ Sale or disposition of substantially all assets
- ☀ Merger

See Nonprofit Transactions Guide at [www.ag.ca.gov/charities](http://www.ag.ca.gov/charities)

# Enforcement Program

- ✱ Investigations, audits and civil litigation
- ✱ Focus: mismanagement and diversion of charitable assets from intended use
- ✱ Multiple sources of jurisdiction
- ✱ Cases selection: developed from complaints received and review of annual filings

# Types of Enforcement

- ✱ Informal contact
  - ✱ Corrective action
- ✱ Administrative subpoena
  - ✱ Assurance of voluntary compliance
- ✱ Civil litigation
- ✱ Criminal charges

# Attending to Governance

- ☀ CA Nonprofit Public Benefit Corporation Law governs board duties and responsibilities
- ☀ Activities and affairs of a corporation must be conducted, and all corporate powers exercised by or under the direction of the board
- ☀ This ultimate decision-making role cannot be designated to anyone else

\*See parts VI and VII of 990, and Guide to New Form 990 at [www.ag.ca.gov/charities](http://www.ag.ca.gov/charities)

# Attending to Governance: Board Duties and Responsibilities

- ★ Statutory standard: a director must perform his/her duties
  - ✿ In good faith
  - ✿ In a manner the director believes to be in the best interest of the organization
  - ✿ With such care, including reasonable inquiry, as an ordinarily prudent person would do in the same position under similar circumstances



# Attending to Governance: Critical Principles

- ✱ Be actively engaged and attentive: ask questions and demand answers!
- ✱ Scrutinize budgets and keep an eye on potential risks
- ✱ Avoid conflicts of interest and self-dealing transactions
- ✱ Scrutinize executive compensation
- ✱ Make sure officers and key employees are doing their jobs
- ✱ Closely examine and monitor fundraising practices and activities

# Caution: Use of Restricted Assets

- ☀ Assets are restricted either by donor designation or content of solicitation
- ☀ Duty to use in accordance with restriction
- ☀ Must be able to account for use in accordance with restriction
- ☀ Avoiding problems:
  - ☀ Segregate
  - ☀ Solicitation language



# Complying with Regulations of Other Government Agencies

- ★ Local jurisdictions may regulate solicitation [see list on Resources page]
- ★ Multi-state solicitation [information available at [www.multistatefiling.org](http://www.multistatefiling.org) ]
- ★ SOS
- ★ FTB
- ★ IRS

# The NIA: Amendments to Supervision Act\*

- ✱ Effective January 1, 2005
- ✱ Amendments to existing law\* re:
  - ✱ Charity registration
  - ✱ Charity governance
  - ✱ Charitable solicitation

\* The Supervision of Trustees and Fundraisers for Charitable Purposes Act [Gov. Code sec. 12580-12599.7]

# The NIA: Amendments to Supervision Act

## ★ Applies to:

### ★ Charitable organizations, including:

- ★ Nonprofit corporations
- ★ Unincorporated associations
- ★ Charitable trustees

### ★ Fundraising professionals, including:

- ★ Commercial fundraisers
- ★ Fundraising counsel

# The NIA: Registration

- ✦ Effective date for initial registration with the Attorney General : within 30 days after initial receipt of property
  - ✦ Property includes money and any other type of real or personal property
- ✦ Registration requires a copy of governing instrument , 1023 and by-laws

\*See Registration Checklist at [www.ag.ca.gov/charities](http://www.ag.ca.gov/charities)

# The NIA: Audit requirement

- ★ Applies to the following entities with \$2 million or more in gross revenue\*

- Nonprofit Corporations
- Unincorporated Associations
- Trusts

[Unless exempt from registration and reporting]

\* \$2 million threshold exclusive of revenue from governmental grants and contracts for services for which an accounting is required

# The NIA: FAQs re Gross Revenue

## ★ Definition

- ★ Follow instructions for Line 12 of IRS Form 990 and Line 12, column (a) of IRS Form 990PF
- ★ Non-cash and one-time contributions, and income from special events are included in definition.

\* Additional FAQs available on the AG website

# The NIA: Independent Audit Requirement

- ✱ Independent audited financial statements must be made available to the Attorney General and the public
- ✱ Includes all statements and notes but NOT the management letter
- ✱ No later than 9 months after close of fiscal year



## The NIA: FAQs re Independent Audit Requirement

- ★ Audited financial statements for years prior to F/Y 2005 do not have to be released to the public
- ★ Extension for filing IRS informational returns does not apply to completion date for audit



# The NIA: Audit Committee Requirement

- ★ If required to conduct independent audit

- ★ Composition

- ★ Appointed by Governing Board
- ★ May be only one person
- ★ Can be non-governing board members
- ★ Cannot include 50% or more of members of Finance Committee
- ★ Whether paid or unpaid, cannot include:
  - ★ Staff members (employees of the charity)
  - ★ President or CEO, Treasurer or CFO

## The NIA: Duties and Responsibilities of the Audit Committee

- ★ Recommend hiring and firing of CPA to the Governing Board
- ★ Confirm that financial affairs are in order
- ★ Review and accept/reject audit
- ★ Approve non-audit services by CPA

# The NIA: Requirement for Board Review of Executive Compensation

- ✱ Must be reviewed and approved by the governing board or authorized board committee at 3 points
- ✱ Compensation review includes benefits
- ✱ Applies to all:
  - ✱ Nonprofit corporations
  - ✱ Unincorporated associations
  - ✱ Trusts

Gov. Code sec 12586(g)

# The NIA: Requirement for Board Review of Executive Compensation

- ☀ Must be reviewed and approved for the following positions:
  - ☀ President or CEO
  - ☀ Treasurer or CFO
  - ☀ Or others with comparable powers and duties

# The NIA: Requirement for Board Review of Executive Compensation

★ Review and approval required at 3 points:

- ★ Initial Hiring of the Officer
- ★ Upon Renewal or Extension of the Employment Term
- ★ Modifying the Compensation

\*Standard is “just and reasonable” compensation  
(Corp. Code sec. 5235)



# The NIA: FAQs re Executive Compensation Review

- ☀ Review required for at-will officers on initial hiring and whenever compensation modified
- ☀ New provision does not supersede existing fiduciary duty of officers, directors and trustees under existing law
- ☀ No review required for staff or officers paid more than president or CEO, and treasurer or CFO but the charity should exercise due care to ensure that the salary is just and reasonable

# Top 8 Ways to Get Investigated

- ✱ Failing to ensure all regulatory filings current
- ✱ Allowing CEO/Executive Director sole control
- ✱ Failing to hold regular board meetings and regularly evaluate performance of CEO/Executive Director
- ✱ Failing to properly record board actions in meeting minutes [and poor record-keeping in general]
- ✱ Failing to implement adequate internal controls
- ✱ Allowing self-dealing transactions without analysis required by law
- ✱ Failing to aggressively monitor fundraiser
- ✱ Failing to ensure restricted gifts used only per donor intent

# Top Excuses That Will Only Make it Worse

- ✱ We've always done it that way
- ✱ I didn't know I had to register/No one told me
- ✱ "So and So" was supposed to do that
- ✱ We're a volunteer board and don't have time to...
- ✱ I completely trusted ...
- ✱ Only our treasurer gets to see the financial records
- ✱ We threw those records away. No one told us we had to keep them

# Commercial Fundraisers

## ★ Definition

- ★ Any individual or entity who does the following for compensation:
  - solicits assets for charitable purposes,
  - receives or controls such solicited assets, or
  - employs any compensated person to do either

Gov.Code sec. 12599

# The NIA: Notice of Intent to Solicit for CFRs

- ☀ Notice to Attorney General
  - 10 working days before the start of a solicitation campaign or event
  - *Exception* for disaster solicitations – provide notice concurrent with commencement of campaign

Gov. Code sec. 12599(h)

# The NIA: Written Contract Requirements for CFR

- ✱ For every solicitation campaign or event
- ✱ Voidable unless the commercial fundraiser is registered with the Attorney General
- ✱ Must be signed by an official authorized by the Charity's Governing Board

# The NIA: Required Provisions in CFR Contracts

- ★ The written contract must contain or state:
  - ★ Charitable Purpose
  - ★ Obligations of both parties
  - ★ Fee arrangement
  - ★ Effective, start, and termination dates
  - ★ 5-day deposit of contributions
  - ★ Charity control of content and frequency
  - ★ Maximum amount to secure attendance, sponsorship or endorsement of an event
  - ★ Cancellation rights

Gov. Code sec. 12599(i)

# Fundraising Counsel

## ☀ Definition:

- ☀ A Fundraising Counsel is any individual or entity who for compensation
  - Plans, manages, consults or prepares material for solicitation of assets for charitable purposes
  - Does not solicit assets for charitable purposes
  - Does not receive/control such assets
  - Does not employ persons who solicit assets or receive/control such assets

GC sec. 12599.1

# The NIA:

## Notice of Intent to Solicit for FRCs

- ★ Notice to the Attorney General
  - ★ 10 working days before the start of a solicitation campaign or event
  - ★ Exception for Disaster Solicitations\*

\*Notice can be made concurrent with commencement of campaign

# The NIA: Written Contract Requirements for FRCs

- ✱ For every solicitation campaign or event
- ✱ Voidable unless the fundraising counsel is registered with the Attorney General
- ✱ Must be signed by an official authorized by the Charity's Governing Board

GC sec. 12599.1(e)

# The NIA: Required Provisions in FRC Contracts

- ★ The written contract must contain or state:
  - ★ Charitable Purpose
  - ★ Obligations of both parties
  - ★ Fee arrangement
  - ★ Effective, start, and termination dates
  - ★ Cancellation rights
  - ★ Charity control of content and frequency
  - ★ Statement that fundraising counsel will not solicit, receive or control donated funds, assets or property or employ another to do so

Gov. Code sec. 12599.1(f)

# The NIA:

## Contract Cancellation Rights

- ★ Applies to all fundraising professionals
- ★ Contract voidable if CFR or FRC not registered with Attorney General
- ★ Right to cancel for any reason w/in 10 days of execution

Gov. Code sec. 12599.3

# The NIA:

## Specific Obligations When Fundraising

- ✱ Do not misrepresent purpose of charity or beneficiary
- ✱ Charity exercise control over fundraising activities
  - ✱ Approval of written contracts
  - ✱ Assure no coercion
- ✱ Commercial fundraisers and charities must all be registered with the Attorney General
- ✱ Transfer of funds to account controlled by charity within 5 days of receipt

Gov Code sec. 12599.6

# The NIA:

## Prohibited Solicitation Acts

- ✱ Any violation of Govt. Code section 12580-12599.7
- ✱ Unfair or deceptive acts or fraudulent conduct
- ✱ Using any name or symbol that falsely suggests a contribution is for a particular charitable organization
- ✱ Misrepresenting that a contribution is for a charitable organization or will be used for a charitable purpose when it is not true



# The NIA: Prohibited Solicitation Acts

- ✱ Representing that a person endorses a charitable solicitation unless that person has agreed to do so in writing
- ✱ Misrepresenting endorsements or characteristics of goods or services
- ✱ Representing that a charity has endorsements or affiliations it does not have



# The NIA: Prohibited Solicitation Acts

- ✱ Representing that registration constitutes an endorsement or approval by the Attorney General
- ✱ Misrepresenting the net proceeds to be received by the charity
- ✱ Issuing items that can be used for display on a motor vehicle that suggest an affiliation with a group of public safety personnel

# The NIA: Prohibited Solicitation Acts

- ✱ Representing that contributions solicited will be given to another charity unless that charity has given prior written consent
- ✱ Representing that event tickets will be donated for use by another person or entity unless:
  - ✱ Written commitments to accept tickets and
  - ✱ Tickets do not exceed those received from the charity or the total capacity of the event site

# The NIA: Record-keeping Requirements for CFRs\*

- ✱ Keep records for 10 years
- ✱ Document all revenue and expenses
  - ✱ Cash: date and amount
  - ✱ Non-cash: date, amount, name and address of donor
  - ✱ Name and address of each employee or agent involved
  - ✱ Bank account numbers, names, locations

GC sec. 12599.7

\*Note: AG has 10 year s/l for charities as well.

# Raffle Regulation Overview

- ✱ A raffle is defined as a lottery
- ✱ History
- ✱ Penal Code sec. 320.5
  - ✱ Creates an exception to California law prohibiting gambling

# What Is A Raffle?

- ✱ Gambling is defined as the purchase of a chance to win a prize
- ✱ Raffle includes:
  - ✱ Paper ticket with identifying number and detachable stub
  - ✱ Drawing held to determine winner

# Raffles

## Limits On Who Can Conduct

- ☀ Must be an “eligible” organization\*:
  - ☀ a private nonprofit organization
  - ☀ qualified to do business in CA for at least one year before raffle conducted
  - ☀ Tax exempt under specific Rev. and Tax Code sections

\*does not include public schools or other government entities

# Raffles

## Annual Registration

- ☀ Must be registered with Attorney General **prior to** conducting raffle:  
September 1 – August 31
- ☀ Separate from registration under Government Code
- ☀ Must have confirmation letter from Registry **before** raffle conducted
- ☀ Each chapter of statewide organization must register separately

*\*Exemption:* nonprofit religious organizations, educational institutions, hospitals, BUT must comply with all other provisions of sec. 320.5

# Raffles Restrictions

- ★ 90% of gross receipts from ticket sales for each draw must either:
  - ★ Be used by the organization conducting the raffle for its charitable or beneficial purpose
  - ★ Or given to another eligible organization to use for its charitable or beneficial purpose

# Raffles

## Restrictions

- ★ Proceeds must be used in California
- ★ Non-restricted funds from sources other than tickets can be used to pay for costs
- ★ None of the 90% restricted funds can be used to compensate a person in connection with operation of the raffle
- ★ Can advertise, but not conduct raffles on the internet.

# Raffles

## Restrictions

- ✱ Cannot use gaming machines to conduct raffles
- ✱ Cannot sell tickets or conduct raffle in a satellite wagering facility, at a racetrack or gambling establishment
- ✱ No legal entity or individual may hold financial interest in the raffle except eligible organization conducting, or receiving proceeds from, the raffle

# Raffles Reporting

- ✱ Separate report for each raffle held
- ✱ Report(s) filed no later than 9/1
- ✱ Reporting requires precise financial records
  - ✱ Total funds received
  - ✱ Total expenses
  - ✱ Charitable or beneficial purpose for which proceeds used
  - ✱ Name of eligible organization receiving proceeds

# Raffles

## Exemption from Regulation

A raffle is exempt if:

- ✱ It involves general and indiscriminate distribution of tickets
- ✱ Tickets are offered on same terms and conditions as tickets for which donation given
- ✱ Participants are not required to pay for a chance to win

Penal Code sec. 320.5(m)

# Recent Developments

- ✱ Registry automation project
- ✱ New 990/990-N for <\$50,000
  - ✱ IRS 3-year revocation project
- ✱ Website resources
  - ✱ Registration guide
  - ✱ Guide to submitting transactions
  - ✱ Guide for Charities
  - ✱ Forms and instructions
  - ✱ Laws and regulations
  - ✱ Model contract
  - ✱ Resources re conduct of raffles



# ATTORNEY GENERAL

## Contacts and Information

- Web resources:  
[www.ag.ca.gov/charities](http://www.ag.ca.gov/charities)
- Specific questions:  
[Belinda.Johns@doj.ca.gov](mailto:Belinda.Johns@doj.ca.gov)